Economist.com

Tuesday May 20th 2008

Special report

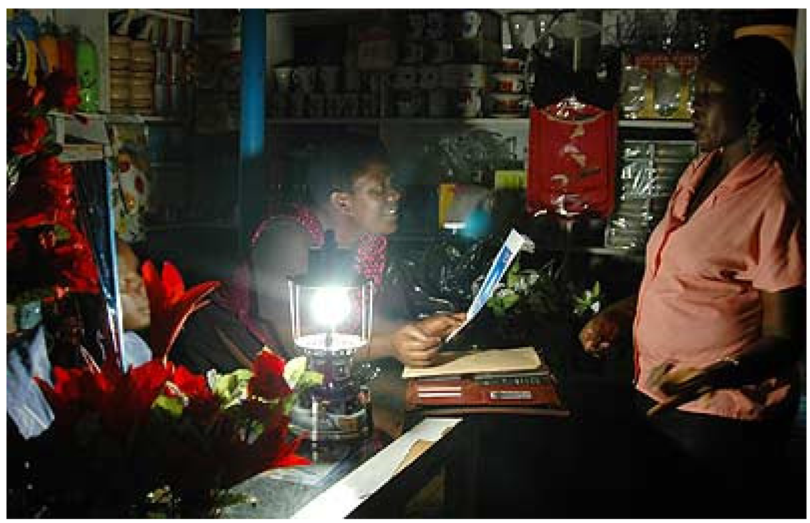
Business in Africa

The flicker of a brighter future

Sep 7th 2006 | JOHANNESBURG, LUANDA AND LUSAKA
From *The Economist* print edition

Once again, Africa is listed as the most difficult place in the wor business. So why are some businessmen happy to be there?

Reuters

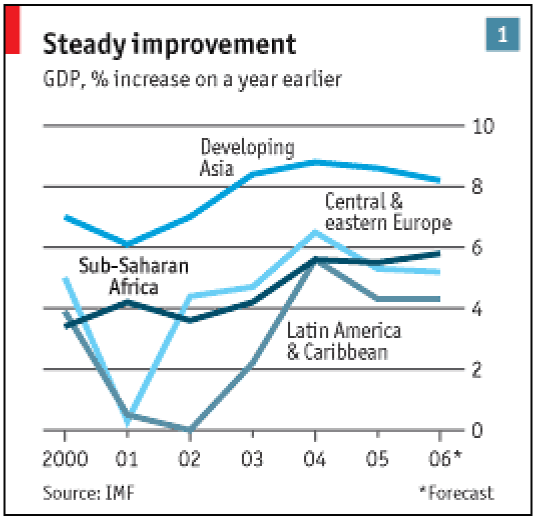


THE prospect of investing in sub-Saharan Africa can cause businessmen to in a cold sweat. The region is often seen as a corporate graveyard of small impossibly difficult markets, where war, famine, AIDS and disaster are alw lurking. This week an annual World Bank study once again named Africa a difficult region in which to do business. But not everyone sees it like that. Mackay, who runs SABMiller, the world's second-largest brewer, has said t there was any more of Africa, we'd be investing in it."

Mr Mackay, whose firm has its origins in South Africa, is one of plenty of b leaders to see opportunities in the continent. Companies are being started successfully built in many African countries, especially in banking, retailing mobile telephones. The region's economy is growing steadily (see chart 1) expand by 5.8% this year. In part this is because of a commodities boom

Home
This week's print edition
Daily news analysis
Opinion
All opinion
Leaders
Letters to the Editor
Blogs
Columns
KAL's cartoons
Correspondent's diary
Economist debates
World politics
All world politics
Politics this week
International
United States
The Americas
Asia
Middle East and Africa
Europe
Britain
Special reports
Business
All business
Business this week
Management
Business education
Finance and economics
All finance and economics
Economics focus
Economics A-Z
Markets and data
All markets and data
Daily chart
Weekly indicators
Currencies
Rankings
Big Mac index
Science and technology
All science and technology
Technology Quarterly
Books and arts
All books and arts
Style guide
People
People
Obituaries
Diversions

forgiveness. But more peace, political stability and better economic manag
have done their bit, too.



Nevertheless, there is a long wa
and still plenty to frighten away
Chad, for instance, recently den
that Chevron and Petronas pay
taxes or face expulsion, even th
companies thought they had me
obligations. The government als
it wants a share in the oil conso
Some companies come up with
complaints. One construction fir
road in a West African country c
have half the work it completed
day destroyed at night by peopl
out steel reinforcements. After s
misfortunes elsewhere, it event
the region.

Doing business in Africa is hard
World Bank study measures things like red tape and taxes. South Africa, M
Namibia and Botswana rank among the best 50 countries in the world. But
least business-friendly, 27 are in sub-Saharan Africa. Some are impossibly
firms paid all taxes due in Sierra Leone, they would spend almost three tin
total profits; in the Democratic Republic of Congo, registering a business ta
days and costs almost five times the average Congolese's annual income c
enforcing a contract in Angola involves 47 procedures and takes over 1,00

For many African entrepreneurs, operating legally brings too many headac
too few benefits. As a result, 42% of the region's economy is informal, the
proportion in the world (see chart 2). This hinders firms from growing and
much-needed employment outside the civil service. In Malawi only 50,000
of a population of 12m have formal jobs in the private sector.

Moving goods across borders takes a lot of patience. At the Chirundu bord
between Zimbabwe and Zambia, an endless line of trucks languishes, wait
sometimes days to clear customs. This keeps African markets small and fra
Ayisi Makatiani, a Kenyan entrepreneur who now helps African businesses,
tape is one of the main problems for business. "The government is a broke
bureaucracy in many places. If they were in business, they would be bankr
sighs.

Bad roads, or a lack of them, add to the difficulties. Reliable electricity is ra
Currency fluctuations are hard to stomach. Purchasing power is in short su
Almost half of the 750m sub-Saharan Africans live on less than $1 a day. T
qualified staff is small. AIDS claims the lives of employees and customers a
according to surveys from Transparency International, a Berlin-based corru
watchdog, graft is still seen as a huge problem. Countries like Côte d'Ivoire
Zimbabwe, once regional powerhouses, have descended into political and e
ruin.

With such a formidable list of ha
wonder many investors stay away. The costs and risks—not to mention the
hardly seem worth it. Africa captures less than 3% of global foreign direct
investment. And most of this is from mining and oil companies, which have
choice but to go where the minerals are.

Audio and video
- Audio and video library
- Audio edition

Research tools
- All research tools
- Articles by subject
- Backgrounders
- Economics A-Z
- Special reports
- Style guide

Country briefings
- All country briefings
- China
- India
- Brazil
- United States
- Russia

Cities guide

Print subscriptions
- Subscribe
- Renew my subscription
- Manage my subscription
- Activate full online access

Digital delivery
- Economist.com subscriptions
- E-mail newsletters
- Audio edition
- Mobile edition
- RSS feeds
- Screensaver

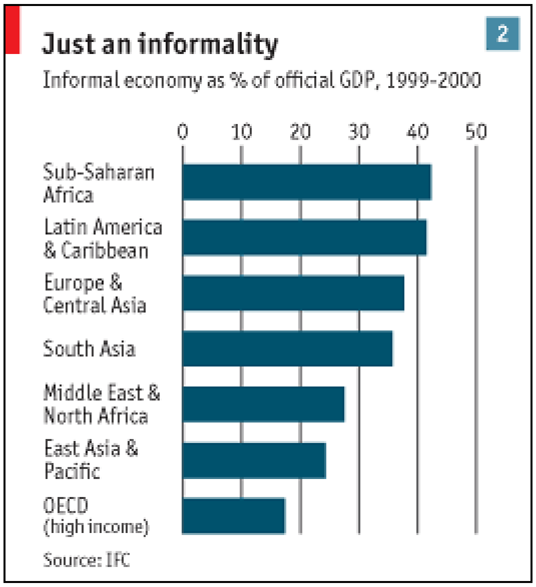
Classifieds and jobs

The Economist Group
- About the Economist Group
- Economist Intelligence Unit
- Economist Conferences
- The World In
- Intelligent Life
- CFO
- Roll Call
- European Voice
- EuroFinance
- Reprints and permissions

Growing a business

EIU online store

Economist shop



Just an informality

Informal economy as % of official GDP, 1999-2000

Source: IFC

Yet some of the entrepreneurs \ manage to succeed in Africa fin rewards are great. When Celtel, phone operator, set up in Zamb years ago, it concentrated on th populated corridor between Vict (on the border with Zimbabwe), and the industrial copper belt. T thought to be the only area in w business. Yet in 2003, the comp decided to invest in rural servic and was astonished at the resul

Although most rural customers used a telephone, they were ke one. This encouraged more peo cities to obtain mobile phones t relatives in the countryside. The introduction of Me2U, a service callers to use text-messaging tc airtime credit to other mobiles, provided a further boost. Most people do n bank accounts and the service has become a convenient and cheap way to money. In villages it has also emerged as a substitute for cash, with peopl airtime to pay for their shopping. Shopkeepers cash in their accumulated p credits with people who make money by offering callers use of their mobile a sort of public phone. Within the past two years, Celtel's Zambian custom grown from 70,000 to over 1m.

Celtel found that it succeeded if it adapted products and services to local t needs and small budgets. A similar adjustment is to be found in Uganda, w SABMiller at first depended on imported malt to make its beer. It develope beer made from cheaper, locally grown sorghum and negotiated a reductic tax. The reduction in costs was used to lower the sale price. The cheaper b resembling lager, sold well and has now been introduced to other countries region. Most drinks are also sold in returnable glass bottles, which are che cans.

Although many Africans are poor, they are willing to pay for what they nee plentiful creativity and entrepreneurship in the informal economy can be h to cater to them. Prepaid telephone cards and soft drinks, often distributed informal networks, can be found in tiny stalls in the most remote corners c despite all the difficulties with transport.

In Ghana Barclays, a British bank, started working with "Susu collectors", savings daily from informal traders without access to banking, to keep the safe. There are an estimated 5,000 Susu collectors in the country, each wo an average of 400 clients. This is a $140m market that exists below the tra banking radar. Barclays now offers special bank accounts, training and len Susu collectors, who can provide credit to their clients. The bank was take the amount of money, sophistication and willingness to save in the informa economy.

Such results take patience and imagination. In Nigeria South Africa's MTN, largest mobile-phone company in the region, had to build its own microwa transmission backbone and power supplies. It now enjoys a 45% market s over 9.6m subscribers. In Uganda it erected the first solar payphone, used fishermen, on Lake Victoria. Many of the rural branches of South Africa's S

Bank rely on satellite transmission, diesel generators and solar power. Its branch on a Lake Victoria island receives money from the sky: with no lan planes drop bags of cash to be collected by staff and security guards. Havi a local bank, improved service and invested in more branches, Standard B serves almost half the Ugandan market.

For such companies, the reward for coping with the risk and the hassle co returns and a lack of competition. Successful businesses can expect to enj comfortable margins, rewarding them for their time and investment. SABM operating margins are in Africa; MTN's are over 42%.

Successful investors say that Africa can be no harder than other emerging but that doing business requires good local knowledge. South African com to be well placed to operate in the region—though Peter Wharton-Hood of Bank cautions that: "You can't have South Africa dumped into Kampala." S believes that its African roots help it better to understand the cultural sens the continent. Dimension Data (Didata), a South African IT company that operates globally, finds emerging markets easier going than the intensivel competitive and unfamiliar European or North American ones.

Finding a local partner helps. Locals may not bring much capital or technic expertise, but their knowledge and networks are invaluable. "You can't arr Nigeria and hope to understand what's going on without a local partner," s McCormack, who is in charge of Africa at Didata. It is also a way of assuag distrust in foreign companies, which are often perceived as mammoths ba make a quick buck or to wreck local businesses. South African supermarke example, have been accused of undermining local traders and snubbing lo suppliers. SABMiller's African operations are joint ventures with locals, som governments. André Parker, in charge of Africa at SABMiller, admits that t always smooth sailing. "It is an educational process for both sides." Manag consensus can be slow, but having local shareholders and the government pays off in the long run.

Employing and retaining clever and resilient people is also tricky. "The dep in Africa is huge," says Standard Bank's Mr Wharton-Hood. Experience is, often thin. Most foreign firms have to spend heavily on training; and persu trained staff to stay is not easy. Besides generous salaries and perks such or medical cover, promises of exciting career prospects—at home and abr be needed to keep people happy.

Size and nationality make a difference, too. Neuma Grobbelaar, who head projects on business in Africa at the South African Institute for Internation think-tank, says large foreign companies are in a much better position tha local ones are to weather Africa's frustrations. They have easier access to they can negotiate exemptions, incentives and tax breaks from governme local companies can only dream of; they can invest time and money in un and navigating Byzantine regulations; and they have enough power to say corruption without getting harassed. Celtel refused to pay its way into the Republic of Congo. This delayed negotiations by two years, but the compa eventually made it.

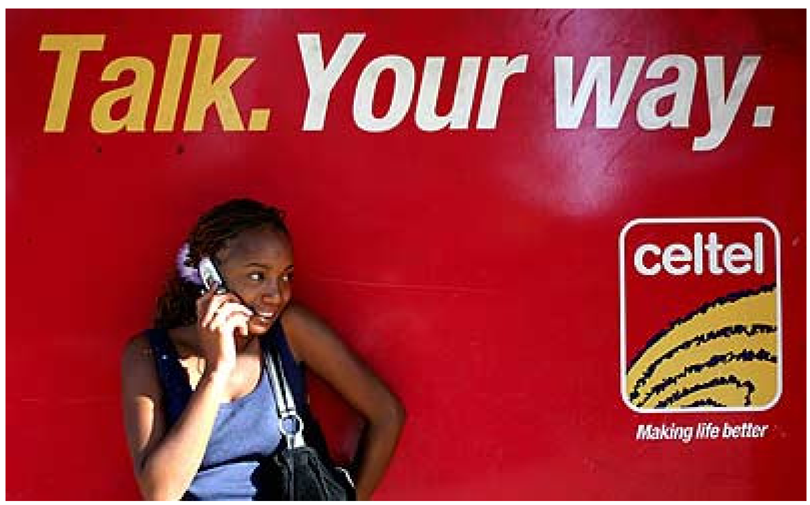
In for the long haul

The time, investment and risk involved in making Africa work mean that i there is not for everyone—which is why profit margins are large. "When w Mozambique, people thought we were mad," recalls Vincent Maphai, who h Billiton in South Africa. In the mid-1990s Mozambique was coming out of a and the area where the company was building its Mozal aluminium smelte infested with malaria. But the mineral resources were valuable and the cor believed in the country's potential. This encouraged other investors, who f BHP Billiton's footsteps into Mozambique, where the economy has grown b average of 8% a year over the past decade.

Foreign investors, especially large ones, are expected to contribute more t and salaries. They must also take care of employees and local people and private sector. Weak and poor governments are often unable to provide se as health care and education, and people want something from foreign inv which often benefits only a small elite. "Don't even dream of doing busines if you're not prepared to leave a visible legacy," says Mr Maphai. "Investin communities is taken for granted. You do not get rewarded for doing it. Yo punished for not doing it." The Mozal plant supported an anti-malaria prog a school. Many foreign companies help employees and sometimes custome with HIV/AIDS.

Such efforts can sometimes help the business. BHP Billiton considers the ti money spent helping local suppliers as a worthwhile investment. Mozal—es account for over 3% of the country's GDP and a third of its economic grow purchases $11m-worth of goods and services a month from over 200 local SABMiller, which relies on local transport to distribute its beers and soft dr remotest corners of Africa, helps entrepreneurs obtain credit, trucks and tr Zambian operation has 1,100 employees, of whom only four are expatriate

Vismedia



Cash call

Last year, large firms with an interest in the region set up Business Action to help foster the private sector. The realisation that much of Africa's deve depends on helping local businesses flourish has resulted in a flurry of initi don't believe for a moment that there is a stronger entrepreneurial spirit ir in Africa," says Ms Grobbelaar. But small informal businesses need to be consolidated, nurtured and brought into the formal economy. Reforms nee life easier not just for large foreign companies, but also for small ones. Bet with the local private sector would also help spread the benefits of foreign investment.

Ultimately, doing business in Africa is a gamble on the future—that the cor make something of the commodity boom that has helped it grow faster in three years than at any time in the past few decades and, possibly, ever. I economy takes off, investors intend already to be there, firmly rooted. "Afr promise is about tomorrow," says SABMiller's Mr Parker. The Thousand Hil Fund, a small private-equity firm set up to invest in Rwanda, is also optimi Fogler, the co-founder, believes that the country has already turned the co wants to prove that investing in small companies in Africa can be successfu his is the only Africa fund based in the United States to be entirely finance private money.

Although African countries have thrown away past opportunities, the optim yet be proved right. Virtually all those countries that once embraced a Mar have now forsaken it; few even call themselves socialist any more. Large p economies have been privatised. Places like Nigeria, Zambia and Rwanda h launched anti-corruption sweeps. Africa may remain at the bottom of the W survey, but it is the third most-reforming region—which it has never been Tanzania and Ghana were amongst the most enthusiastic reformers in the year. Nigeria has embarked on a reform of the courts. In Kenya traders ca custom duties online, reducing time and hassle. Keen to see their ranking some governments have been jolted into action and are now talking to the sector to identify the most-needed reforms.

Will it last? Michael Klein, in charge of private-sector development at the W thinks it could. If governments remain on their current track, he believes G in sub-Saharan Africa could reach 9% in a decade or so. That is a brave pr a region prone to booms and busts, because of its reliance on minerals, oil Previous commodity booms have been squandered and in some cases, ofte of complacency, left countries in an even worse mess. This could happen a with better fundamentals, Africa may now be more resilient than it was. Fo thing, African oil importers are coping with high prices much better than th the 1970s.

Foreign investors are governed by trust. India and China also rank relatively poorly in the World Bank survey, but are nonetheless investment magnets. Mr Klein argues this is because investors are confident that these countries are going in the right direction and they want to tap into their large markets early. Africa will have to prove itself through years of good performance and sustained reform before it can gain such confidence. But if it does, those who are already betting on the continent will be miles ahead.

Back to top ^^